

UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In Chapter 11 proceedings

Case Nos. 98-12547
through 98-12570-PHX-C'GC
Jointly administered

Adversaw No. 2-05-ap-00299

Plaintiffs,

VS.

**UNDER ADVISEMENT RE:
MOTION TO COMPEL; MOTION FOR
INJUNCTIVE RELIEF; MOTION FOR
SANCTIONS**

Defendants.

On August 20, 2005, this Court issued its Under Advisement Decision Re: Mntions to Dismiss filed by Defendants ACE Insurance Company, Ltd. ("ACE"), Bailey Cavallieri, LLC, Dan Bailey, and Conyers Dill & Pearman against Plaintiffs.¹ ACE is a Bermuda insurance company that issued a D&O policy at Debtor Boston Chicken, Inc.'s request insuring Debtor's directors and officers from loss. After confirmation of Debtor's Plan, the Plan Trustee Gerald K. Smith commenced litigation against various parties, including the D&O's. Some of the insured D&O's

"The decision was docketed on Saturday, August 20th, but not officially noticed out to the parties until August 22nd, the following Monday, due to the Court being closed over the weekend. However, all parties were notified telephonically on Friday, August 19th, to check the docket over the weekend for the decision to be rendered and available for the parties' review. There appears no dispute that all parties to the Bermuda proceedings on Monday, August 22nd, had seen and read the decision before the Bermuda hearing.

1 settled and assigned their rights against ACE to the Plan Trustee.

2 In an apparent effort to preempt the Plan Trustee from proceeding against it in this country,
3 ACE, through its Bermuda counsel Conyers, Dill & Pearman (“Conyers”), filed an action in the
4 Supreme Court of Bermuda against the Plan Trustee and settling D&O’s (“the Bermuda Action”)
5 seeking an *ex parte* injunction, which the Bermuda court granted that day. ACE also sought to
6 commence arbitration of all disputes in Bermuda under a provision in the insurance policy.

7 Subsequently, Plaintiffs brought this action against ACE, Conyers and its United States
8 coverage counsel, Bailey Cavalieri, LLC and Dan Bailey (jointly “Bailey”), seeking an injunction
9 to stop the Bermuda proceedings, contempt, contract damages, declaratory relief, and bad faith
10 damages.² Defendants then sought to dismiss the case on a variety of grounds, which necessitated
11 the Court’s August 20, 2005, decision. In that decision, this Court held that it has personal
12 jurisdiction over ACE under the principles of *Int’l Shoe Co. v. State of Washington*, 326 U.S. 310
13 (1945), *McGee v. Int’l Life Ins. Co.*, 355 U.S. 220 (1957), and *Asahi Metal Industry Co. v. Superior*
14 *Court of California*, 480 U.S. 102 (1987).³ The Court also concluded that to the extent this case
15 implicates the insurance policy specifically identified as property of the estate and its proceeds, the
16 Court has *in rem* jurisdiction and, under the plan and 28 U.S.C. § 1334(c), that jurisdiction is
17 exclusive. It further concluded, however, that *in rem* jurisdiction does not extend to the bad faith
18 claim asserted or to the damage claims for violation of *Barton*. In those causes of action, this Court
19 held, “more is sought than a determination of rights in a *res*; rather, the Trustee seeks a judgment for
20 personal liability beyond the boundaries of the *res*. For those claims, the Trustee must rely on *in*
21 *personam* jurisdiction to proceed.”

22 The Court also addressed the question of arbitrability of the insurance policy and concluded
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25 ²For additional background facts not immediately germane here, see this Court’s August 20, 2005
Under Advisement Decision.

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27 ³Under the same principles, however, the Court concluded that it did not have personal
jurisdiction over Conyers, ACE’s Bermuda counsel, and therefore dismissed this adversary as to
28 Conyers solely. The Court denied, however, Bailey’s motion to dismiss.

1 that, “outside bankruptcy, the arbitration clause . . . should be enforced and that all issues, including
2 policy exclusions, exhaustion of senior coverages, repudiation, and bad faith, would be within the
3 scope of the arbitration proceeding.” Debtor’s bankruptcy, however, creates an obligation under
4 *Barton v. Barbour*, 104 U.S. 126 (1881), requiring leave of court before a trustee may be sued. This
5 Court highlighted the fact that the *Barton* doctrine does not bar suits, arbitrations or other
6 proceedings, but merely requires leave of the appointing court *in advance* of the filing of suit.
7 Further, whether leave should be granted is based on “any conflicting considerations over what is
8 the best place to determine a particular dispute after being fully informed on those issues by all
9 parties.”

10 At the time of this Court’s August 20th, 2005, decision, Defendants had not yet sought leave
11 of this Court to pursue the Trustee and, therefore, the question of whether leave should be granted
12 was not yet in fact ripe for consideration. However, the Court did decline at that point to defer to
13 the Bermuda court under principles of comity until ACE complied with the *Barton* doctrine and
14 properly sought leave of this Court first. In a nutshell, that is where the parties find themselves today
15 – before this Court on ACE’s request to compel arbitration or, in the alternative, for leave to proceed
16 in Bermuda.

17 Immediately following the Court’s August 20th decision, the parties appeared before the
18 Bermuda court on the Trustee’s motion to dismiss the Bermuda action. Defendants did not, as a
19 result of this Court’s decision, voluntarily dismiss the Bermuda case, but in fact defended themselves
20 against dismissal of the Bermuda case. The Trustee complains that Defendants’ failure to dismiss
21 the case and their continuing argument to the Bermuda court that this Court’s ruling was wrong, that
22 this Court does not have jurisdiction over Defendants and that the *Barton* doctrine does not apply
23 shows an ongoing violation of *Barton* and contempt of this Court. Further, the Trustee contends that
24 Defendants sought affirmative relief at the hearing on the Trustee’s motion to dismiss and in fact
25 received affirmative relief against the Trustee in those proceedings. For this, the Trustee seeks
26 contempt sanctions against Defendants and an injunction requiring Defendants to dismiss with
27 prejudice the pending Bermuda action and be enjoined from filing any legal proceeding, suit or claim
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1 against the Trustee without first seeking this Court's approval.⁴ Additionally, the Trustee requests
2 this Court deny Defendants' motion to compel arbitration and/or leave of court on principles of
3 unclean hands and judicial estoppel.

4 **II. Discussion**

5 **A. The *Barton* Doctrine and the Motion to Compel**

6 ACE apparently views its present motion as an attempt to satisfy *Barton*, but in reality it reads
7 like a motion to reconsider the Court's previous rulings. The gist of ACE's argument is that it
8 bargained for arbitration in Bermuda and it should get what it bargained for.

9 Unfortunately, this continues to miss the point. The application of *Barton* may often infringe
10 on a party's rights because of the special rights of the trustee. See *In re Crown Vantage, Inc.*, 421
11 F.3d 963 (9th Cir. 2005). So the issue becomes how to balance the "conflicting considerations"
12 between arbitration in Bermuda and legal proceedings in a United States bankruptcy court in
13 determining where and how this dispute should be resolved. ACE offered scant help on this score
14 in its papers, although counsel did suggest at oral argument that it would be amenable to arbitration
15 somewhere else (so long as it is not the United States) and that the timing of the arbitration could be
16 adjusted in light of the Trustee's pending litigation obligations in the District Court of Arizona.

17 Just as ACE's position on this point is unenlightening, the Trustee's is overzealous. Any
18 violation of *Barton* can be addressed adequately without stripping ACE of its contractual right to
19 arbitrate; the Trustee's "unclean hands" argument is unavailing to the contrary. The best thing to do
20 at this point – in an effort to put an end to the ping pong multinational litigation currently underway
21 – is to determine whether or under what terms the arbitration clause should be enforced. In short, the
22 inquiry should now be, treating ACE's current motion as a motion under *Barton* to allow the
23 arbitration to continue: should that motion be granted, and if so, under what conditions?

24 The essence of *Barton* is to protect the trustee in his administration of the estate. This
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26 ⁴The Trustee also complains that Defendants have really been in violation of the *Barton* doctrine
27 since filing the Bermuda case back in March of 2005, which is also when the Trustee notified
28 Defendants of *Barton*.

1 includes protecting him from having to defend multiple suits in different venues to the detriment of
2 the estate and to protect this Court's jurisdiction over the *res* of the estate. However, the Trustee
3 takes the assets as they are. Here, a key characteristic of this asset -- the insurance policy -- is the
4 agreement to arbitrate; that agreement is not stripped away because the Trustee is now the real party
5 in interest. In this sense, ACE's "bargained for" rights argument does make sense; the agreement to
6 arbitrate is part of the bundle of rights on both sides to which the original parties agreed. As
7 previously indicated, the Court has already determined that, outside of bankruptcy, all of the issues
8 presented would be within the purview of the arbitration clause. For the reasons previously stated,
9 the Court continues to believe that submitting these issues to arbitration is the correct result; therefore,
10 ACE's motion to compel will be granted but only on the terms set forth in this decision. This is
11 because *Barton* gives this Court jurisdiction to determine under what conditions that agreement may
12 now be given force. Those conditions may include timing, location, expense, and order of arbitration.

13 **Timing:** At the least, the Trustee is entitled to protection from having to arbitrate while he is
14 focused on pending litigation against the remaining parties in the district court litigation. Therefore,
15 the arbitration will be stayed for a period of six months. As the expiration date approaches, the matter
16 will be set for hearing upon request by either party. If the district court litigation is fully resolved
17 prior to the expiration of six months, it will be the obligation of Trustee's counsel to notify the Court so
18 that a hearing may be set to consider dissolving the stay.

19 **Location and expense:** ACE has made it clear that its primary concern is that the arbitration
20 occur outside of the United States. On this issue, ACE will be given a choice. If the arbitration
21 occurs either in Phoenix or New York (the two US locations suggested to date), each side will bear
22 its own expenses (except to the extent, if any, that a fee or cost allocation award is made as part of
23 the arbitration award). If the arbitration occurs in Bermuda or another mutually agreed upon non-US
24 venue, ACE will be responsible for the incremental costs incurred by the Trustee in the form of travel,
25 accommodation, or venue related legal fees and costs. The Trustee will be responsible in the first
26 interest to delineate those incremental costs in good faith consistent with the intent of this Order and
27 ACE will be responsible to review and approve them in the same spirit. If any dispute on the
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1 incremental fees is brought to this Court for decision, the non-prevailing party will be responsible for
2 the fees and costs incurred to resolve the dispute.

3 **Order of arbitration:** The Trustee has requested that this Court micro-manage the arbitration
4 by instructing the arbitrators on what issues to consider in what order. The Court declines to do so.

5 **B. The Motion for Injunction**

6 With this Order, there should be no continuing argument by ACE that the Bermuda litigation
7 continue. Therefore, it will be enjoined from further prosecuting that case and will be mandatorily
8 enjoined to take such steps as are necessary to dismiss it. Any future issues concerning enforcing the
9 agreement, appointing a third arbitrator, or the like will lie within the jurisdiction of this Court. This
10 result is fully supported by application of the *Kashani* factors cited with approval by the Ninth Circuit
11 in *Crown*.

12 **C. The Motion for Sanctions**

13 The Defendants' conduct in this matter is troublesome. There is no doubt that ACE and its
14 counsel were aware of the Trustee's claim that *Barton* applied. Defendants chose to take the position
15 that it did not. That position proved to be incorrect; as this Court has found. Defendants' conduct in
16 bringing the Bermuda case violated *Barton*. Defendants further ignored *Barton* and this Court's
17 decision by not dismissing the Bermuda case. There is no doubt that this was a conscious course of
18 conduct, prompted, at least in part, by ACE's overriding goal of not submitting to United States
19 jurisdiction and avoiding any conduct that could be interpreted as doing business in this country.
20 Given the conscious and continuing nature of the conduct, sanctions are appropriate.

21 The question is therefore what is an appropriate level of sanction. Once the applicability of
22 *Barton* had been established by this Court's August 20th ruling, ACE proceeded in Bermuda at its own
23 risk. Before then, the Trustee had been required to engage local counsel in Bermuda and hire Ralph
24 Mabey as an expert on U.S. bankruptcy law. These expenditures would clearly have been
25 unnecessary if ACE had taken the simple expedient of proceeding first to seek *Barton* relief. In
26 addition, the expenses of attending the hearing in Bermuda would have been avoided. However, it
27 chose instead to run the risk of being wrong and the case law is clear that sanctions are appropriate
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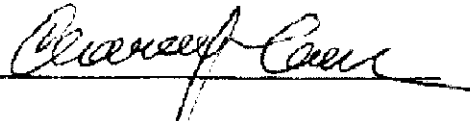
1 for this type of wilful behavior.

2 On the other hand, the positions of Beus Gilbert and the Trustee are different. While both
3 expended time in connection with the ACE matters, neither was specifically engaged to do so. In
4 addition, the fact is that Beus Gilbert is engaged in these matters on a contingency basis (see footnote
5 8 to the Motion for Sanctions). Under the circumstances here, the Court concludes that the
6 appropriate measure for sanctions is the incremental cost incurred by the estate as noted above. These
7 total \$100,000, including a factor for travel and lodging costs incurred in connection with the
8 Bermuda hearing. Therefore, sanctions of \$100,000 will be imposed.

9 Trustee's counsel is to lodge a form of order.

10 So ordered.

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12 **DATED:** January 10, 2006

13 
14 Charles G. Case II
United States Bankruptcy Judge

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16
17 Copy of the foregoing will be sent via facsimile on
18 January 10, 2006, to:


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